

**REPORT ON SIGNIFICANT FINANCIAL
TRENDS AND FINDINGS IN
2011-12 FISCAL YEAR AUDITS OF
DISTRICT SCHOOL BOARDS**



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REPORT ON SIGNIFICANT FINANCIAL TRENDS AND FINDINGS IN 2011-12 FISCAL YEAR AUDITS OF DISTRICT SCHOOL BOARDS

SUMMARY

This report provides a summary of significant financial trends and findings identified in the audits of the 67 district school boards. For the 2011-12 fiscal year, audits of 47 school districts were performed by our office and audits of 20 school districts were performed by other independent certified public accountants (CPAs). The audit reports prepared by the other independent CPAs were required to be filed with us no later than March 31, 2013.

Significant Financial Trends

- At June 30, 2012, school districts Statewide had an average level of general fund total assigned and unassigned fund balance that was 12.24 percent of general fund revenues (financial condition ratio), which represents a 2.23 percent decrease compared to the average financial condition ratio for the previous fiscal year. Of the 67 school districts, three had ratios that were below 3 percent at June 30, 2012. In these circumstances, these school districts had significantly less resources available for emergencies and unforeseen situations than other school districts.

Significant Findings

- The audit reports for 62 of 67 school districts included audit findings addressing weaknesses in internal control; instances of noncompliance with applicable laws, rules, or regulations; or additional matters. Audit reports of eight school districts included one or more findings considered to be material weaknesses, which represents an increase compared to the five audit reports that included material weaknesses for the previous fiscal year. Of the eight audit reports, one also cited instances of material noncompliance.

BACKGROUND

Sections 11.45 and 218.39, Florida Statutes, provide for audits of district school boards to be performed annually by the Auditor General or by other independent CPAs. The scope of these audits includes an examination of the financial statements, the issuance of a report on compliance and internal control in accordance with generally accepted government auditing standards, and the issuance of a report on compliance and internal control relative to Federal awards in accordance with United States Office of Management and Budget Circular A-133.

Section 11.45(7)(f), Florida Statutes, requires that we annually compile a summary of significant financial trends and findings identified in school district audit reports.

FINANCIAL TRENDS

Section 11.45(7)(f), Florida Statutes, along with other inquiries, evidences that critical interest exists to understand and address factors that affect the financial condition of school districts. The financial condition of school districts can be assessed by a review of the general fund balances and activities, which account for the majority of the operating resources and expenditures for K-12 educational programs. Consequently, the general fund is used as the primary basis for measurement of financial condition.

Financial Condition Trends

The financial condition measure used in this report is the ratio of the general fund total assigned and unassigned fund balance to the general fund total revenues (see Exhibit 13). The average financial condition ratio¹ was 12.24 percent at June 30, 2012, which represents a 2.23 percent decrease compared to the average financial condition ratio for the previous fiscal year. The notable financial condition ratio increases for the 2009-10 and 2010-11 fiscal years were primarily due to the school districts’ receipt and use of American Recovery and Reinvestment Act (ARRA) and other Federal economic stimulus funds for certain allowable operating expenditures. The Florida Department of Education (FDOE) required school districts to account for these funds in special revenue funds, rather than the general fund. As discussed in the **American Recovery and Reinvestment Act and Other Federal Funding** section, with the exception of the Race-to-the-Top and School Improvement grants, most ARRA funding terminated during the 2010-11 fiscal year. Exhibit 1 shows the average financial condition ratios for the 2007-08 through the 2011-12 fiscal years.

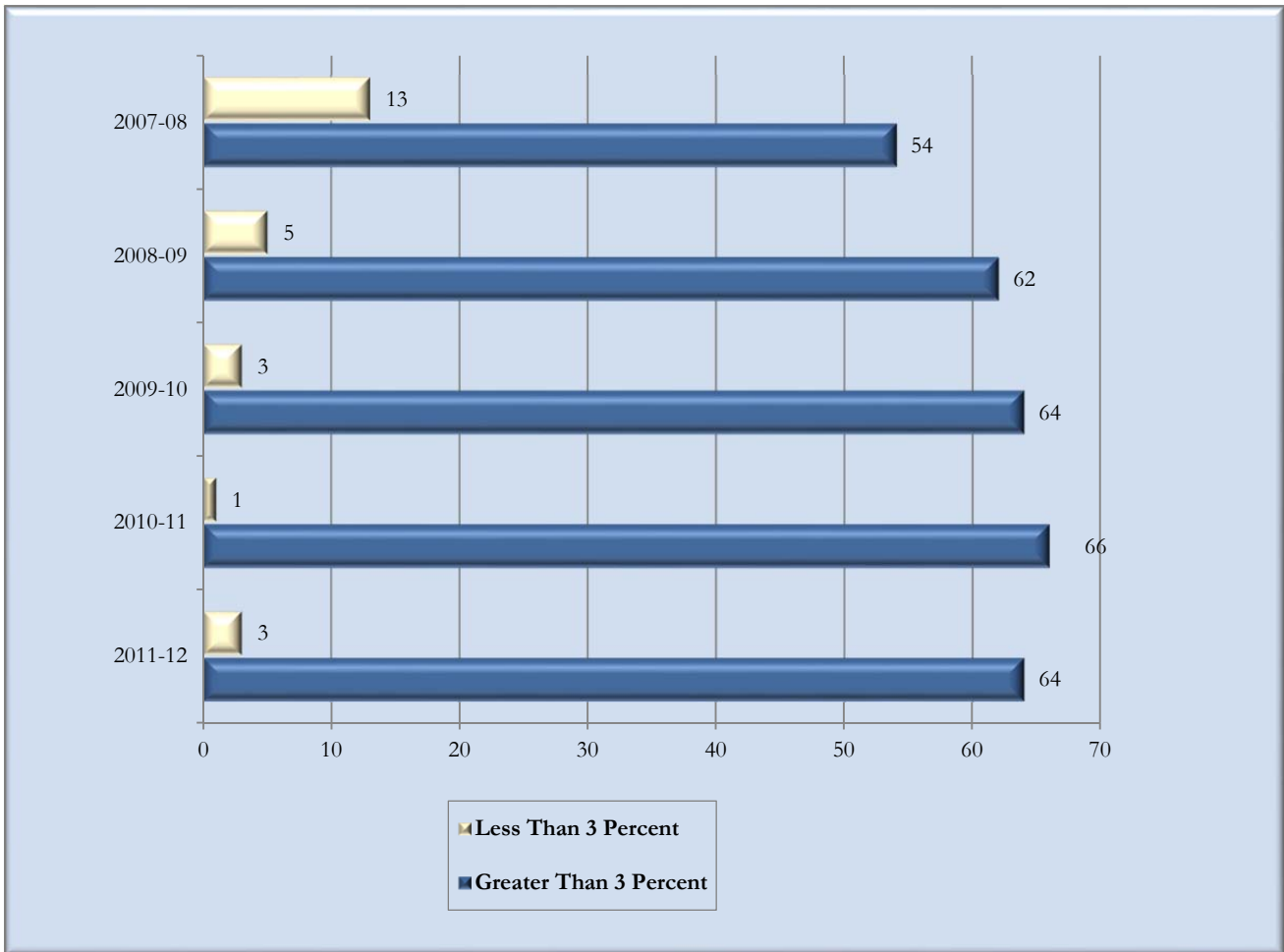
Exhibit 1
Average Financial Condition Ratios of School Districts for 2007-08 Through 2011-12 Fiscal Years



Section 1011.051, Florida Statutes, requires that each school district maintain a general fund ending fund balance that is sufficient to address normal contingencies. If at any time the financial condition ratio determined from the school district’s approved operating budget is projected to fall below 3 percent during the current fiscal year, school district superintendents must notify the Commissioner of Education and respective school board. For consistency with this statutory requirement, Exhibit 2 shows the number of school districts with ratios below 3 percent for the 2007-08 through 2011-12 fiscal years.

¹ For comparison purposes, unassigned/assigned fund balance classification pursuant to Governmental Accounting Standards Board (GASB) Statement No. 54 is similar to unreserved fund balance used in calculating the financial condition ratio prior to the 2010-11 fiscal year. See Exhibits 12 and 13.

Exhibit 2
Number of School Districts with Financial Condition Ratios
Above and Below 3 Percent for 2007-08 Through 2011-12 Fiscal Years



As indicated on Exhibit 2, the number of school districts with financial condition ratios below 3 percent at fiscal year-end decreased over the past four fiscal years to three school districts at June 30, 2012, including one school district that had a deficit ratio at June 30, 2012. These three school districts have significantly less resources available for emergencies and unforeseen situations than other school districts. In addition, Exhibit 3 identifies the financial condition of these school districts and the number of consecutive years that their financial condition ratio was below 3 percent.

**Exhibit 3
School Districts with Financial Condition
Ratios² Below 3 Percent**

School Districts	Financial Condition Ratios - 06-30-2012	Number of Consecutive Years Ratio Below 3%
Columbia	1.62%	1
Franklin	2.13%	1
Manatee	-1.69%	5

The financial condition ratios of several other school districts were below the above-noted threshold at certain times during the 2007-08 through 2011-12 fiscal years, but not at June 30, 2012. Historically, school districts that experience a weak financial condition implement measures that generally restore their financial condition to a favorable position within one or two fiscal years.

If at any time a school district’s financial condition ratio, determined from the school district’s approved operating budget, is projected to fall below 2 percent, Section 1011.051(2), Florida Statutes, requires that school boards have a reasonable plan to avoid a financial emergency, or the FDOE will appoint a financial emergency board to implement measures to assist the school board in resolving the financial emergency. Pursuant to Section 218.503(3), Florida Statutes, a school district is considered to be in a state of financial emergency if the FDOE determines that the school board needs State assistance to resolve or prevent a financial emergency condition.

Factors Impacting Financial Condition

As previously discussed, the 2009-10 and 2010-11 fiscal year financial condition ratios were significantly impacted by the receipt and use of ARRA and other Federal economic stimulus funding, most of which terminated during the 2010-11 fiscal year. Further analyses of school district financial trend data identified other factors that impact the financial condition of school districts and may increase the risk of weak financial condition. While no single factor is identified as a guaranteed predictor of financial condition, factors such as declining property values, increasing or declining enrollment, and school and class sizes require the exercise of effective financial management to limit the impact on the school districts’ financial condition.

Declining Property Taxes. Property taxes are the primary source of local revenues for school districts, and as part of the overall general economic decline, property values have decreased Statewide. According to the Florida Department of Revenue, Statewide property values declined from \$1.6 trillion in the 2009 calendar year to \$1.4 trillion in the 2012 calendar year, a decrease of 12.5 percent. As a result, Statewide property tax levies for school district operations declined from \$12.1 billion for the 2008-09 fiscal year to \$10.4 billion for the 2011-12 fiscal year, a decrease of 14.05 percent.

Increasing Enrollment. Statewide enrollment increased slightly from 2,617,215 for the 2007-08 fiscal year to 2,632,614 for the 2011-12 fiscal year. A total of 26 school districts experienced enrollment growth during this period,

²GASB Statement No. 54 provides that the inventory amount be included in the amount reported as nonspendable fund balance and excluded from the amount reported as unassigned fund balance. Also, nonspendable investments, such as State Board of Administration Fund B Surplus Funds Trust Fund (Fund B), are typically reported in the amount reported as nonspendable fund balance and excluded from the amount reported as unassigned fund balance. For purposes of Exhibit 3, Manatee School District did not classify all inventory as nonspendable and included inventory and Fund B investment amounts in the amount reported as unassigned fund balance, the ratio calculation was adjusted to reduce the unassigned fund balance amount to exclude inventory and Fund B investment amounts because such reporting results in a more conservative presentation of unassigned fund balance.

including 10 school districts for which enrollment growth exceeded 1,000 full-time equivalent (FTE) students, as shown on Exhibit 4. Although these school districts experienced an increase in FTE-based revenue for the increased enrollment, revenue increases can lag behind school district expenditures when staffing new schools and paying initial start-up costs. Also, there is a risk that rapidly growing school districts may overestimate FTE when making FTE projections. Not only are these overestimates costly when FTE-based revenues are adjusted (reduced), but school districts may have made costly hiring and other expenditure decisions based on the estimated enrollment projections.

**Exhibit 4
School Districts with Enrollment Growth
From 2007-08 to 2011-12 Fiscal Years**

Number of School Districts		Unweighted FTE		Increase
		2007-08	2011-12	
1	Orange	171,488.44	178,847.25	7,358.81
2	Palm Beach	169,260.32	175,083.70	5,823.38
3	Hillsborough	190,800.43	195,579.40	4,778.97
4	Lee	79,094.60	82,720.40	3,625.80
5	St. Johns	27,737.19	31,355.54	3,618.35
6	Miami-Dade	344,868.72	347,661.28	2,792.56
7	Osceola	51,913.41	54,192.81	2,279.40
8	Manatee	42,072.05	44,136.01	2,063.96
9	Polk	93,015.26	94,629.19	1,613.93
10	Duval	124,834.80	126,076.99	1,242.19

Declining Enrollment. While enrollment slightly increased in total for all school districts from the 2007-08 fiscal year to the 2011-12 fiscal year, 41 school districts experienced enrollment declines during this period, including 6 school districts for which enrollment declines exceeded 1,000 FTE students, as shown on Exhibit 5. Variations in student enrollment and the related impact on funding from year to year can make school district planning and budgeting decisions for staffing and other activities more challenging. In particular, smaller school districts may experience difficulty with gradual enrollment declines, as it is difficult to reduce the number of instructional staff because often no one grade or class within an individual school may be affected enough to justify the reduction.

**Exhibit 5
School Districts with Declining Enrollment
From 2007-08 to 2011-12 Fiscal Years**

Number of School Districts		Unweighted FTE		Decrease
		2007-08	2011-12	
1	Pinellas	107,220.52	102,602.72	(4,617.80)
2	Volusia	64,146.45	61,402.83	(2,743.62)
3	Brevard	73,458.63	71,042.29	(2,416.34)
4	Charlotte	17,452.87	16,214.26	(1,238.61)
5	Seminole	65,015.20	63,842.88	(1,172.32)
6	St. Lucie	39,902.49	38,767.11	(1,135.38)

Number and Sizes of Schools. Considerable variation exists in the number and size of schools. Some school districts have a predominantly larger number of schools, and some have a predominantly smaller number of schools. Additionally, some have varying combinations of large, medium, and small school sizes. Logically, larger schools cost less per student than smaller schools because the salary, benefits, and fixed costs are spread over a larger number of students. We do not intend to suggest that smaller schools are inappropriate; rather, that the number and sizes of schools are relevant factors that impact financial condition among school districts.

Future Financial Trends Considerations

Economic Downturn. The weakness in Florida's economy for the last few fiscal years has resulted in State funding reductions. For the 2011-12 fiscal year, the base Florida Education Finance Program (FEFP) allocation was \$3,479.22 per FTE student, which represents a decrease of \$144.54 from the FTE FEFP allocation of \$3,623.76 for the 2010-11 fiscal year. Conversely, based on the 2012-13 fiscal year FEFP Fourth Calculation released by the FDOE in April 2013, the per FTE FEFP allocation for the 2012-13 fiscal year is expected to increase by \$103.76, from the 2011-12 fiscal year final allocation, to \$3,582.98. FTE in school districts increased by approximately 19,000 from the 2010-11 fiscal year to the 2011-12 fiscal year, and based on the 2012-13 FEFP Fourth Calculation, FTE increased further, by approximately 24,000, in the 2012-13 fiscal year. While these are relatively significant increases compared to recent years, effective financial monitoring and timely and appropriate adjustments to operations are critical to school districts to ensure that the costs of operations remain within available financial resources.

Florida Retirement System. Florida law and rules establish the eligibility, contribution, and benefit requirements for participation in the State-administered Florida Retirement System (FRS), and school district employees are eligible to enroll as members of the FRS. Effective July 1, 2011, most members of the FRS were required to start contributing 3 percent of their compensation to the FRS, which was previously contributed by employers. Also, on that date, employer contribution rates to the FRS declined significantly, such as the FRS regular class employer contribution percentage, which declined from 10.77 percent to 4.91 percent, or a 54 percent decrease. The combination of these factors resulted in a substantial reduction in school district payroll costs. While the 2012-13 fiscal year regular class employer contribution rate increased slightly to 5.18 percent, this remains well below the 2010-11 fiscal year rate of 10.77 percent.

Debt and Other Long-Term Financing. School districts may finance capital outlay projects by issuing long-term debt such as general obligation bonds and school district revenue bonds and by entering into long-term lease finance arrangements generally referred to as certificates of participation. The long-term debt and other financing obligations reported as outstanding as of June 30, 2012, consisted primarily of: Certificates of participation (COPs) totaling \$13 billion; Qualified School Construction Bonds (QSCBs), Qualified Zone Academy Bonds (QZABs), and Build America Bonds (BABs) totaling \$945 million, \$283 million, and \$102 million, respectively; and school district revenue, State Board of Education, and general obligation bonds totaling \$925 million, \$500 million, and \$168 million, respectively. In addition, school districts had \$71 million in long-term debt notes. Generally, school districts extinguish their debt through various pledged resources such as capital outlay millage, discretionary sales surtax, pari-mutuel distributions, and other tax proceeds. As of June 30, 2012, pledged resources were sufficient to cover the required debt service by school districts. However, given the impact of the economic downturn on revenue sources, such as sales tax and property assessments, school districts will need to closely monitor the impact on required debt service payments.

Further, in an effort to reduce overall borrowing costs, eight school districts that issued variable interest rate COPs entered into 22 interest rate swap agreements. The objective of an interest rate swap agreement, a type of hedging

derivative, is to achieve lower borrowing costs by synthetically fixing interest rates on the debt as compared to issuing regular fixed-rate debt. Debt service payments fluctuate, depending on changes in the underlying interest rates linked to the interest rate swap agreements, and accounting standards require that hedging derivatives be disclosed at fair value as of the financial reporting date.

The fair value of an interest rate swap agreement is the estimated amount the school district would have received or paid if the swap agreement was terminated. As of June 30, 2012, total fair values of the interest rate swap agreements for each of the eight school districts ranged from negative \$1.6 million to negative \$139 million. However, the 22 interest rate swap agreements are associated with COPs with remaining terms that exceeded 20 years, and the actual benefit or additional costs of the swap agreements generally will not be known until the COPs have been paid off. Depending on the fair value of the swap agreements upon termination, there is a risk that the debt service costs of these school districts may exceed the costs that could have been experienced from regular fixed-rate debt. As of June 30, 2012, each of these school districts had sufficient available resources to meet their respective debt service requirements.

American Recovery and Reinvestment Act and Other Federal Funding. The distribution of \$5 billion dollars of ARRA funds to the school districts' K-12 programs began in the 2008-09 fiscal year, with the overall goals of improving schools and achievement and producing better results for students. ARRA had a significant financial impact for the 2009-10 and 2010-11 fiscal years on school districts with funding amounts for State stabilization, Federal Special Education, and Federal Title I programs of \$2.7 billion, \$647 million, and \$491 million, respectively, as of June 2011. Further, ARRA competitive grants have been made available to school districts, the largest being Race-to-the-Top Incentive grants. With the exception of the Race-to-the-Top Incentive and School Improvement grants, ARRA funding generally terminated during the 2011-12 fiscal year. In addition, although the Education Jobs Fund grant is not ARRA funding, it is nonrecurring and terminated in the 2010-11 fiscal year.

ARRA mandates special accountability and transparency requirements regarding Federal economic stimulus funds. To support the most effective use of the funds and measure results, recipients are required to report quarterly expenditures tied to the assurances, principles, and strategies associated with ARRA Federal programs. Beginning in October 2009, school districts have had to meet this reporting requirement by the fifth day of each month following the end of the quarter. The necessary information to be reported includes, for example, project descriptions, activity descriptions, job creation and retention data, infrastructure information, subrecipient information, recipient area of benefit information, and population data. For the 2011-12 fiscal year, school districts incurred ARRA and other Federal economic stimulus expenditures totaling \$229 million, a significant decrease compared to the \$1.9 billion expended for the 2010-11 fiscal year.

School District Trends

Funding Trends. School district governmental funds include the general fund, special revenue funds, debt service funds, and capital projects funds. School districts frequently have fiduciary funds (agency and trust funds) and proprietary funds (primarily internal service funds that account for such activities as self-insurance programs). However, substantially all of a school district's resources are accounted for in the governmental funds. Exhibit 6 shows that school districts reported revenues of \$24 billion in the governmental funds for the 2011-12 fiscal year, a decrease of \$2.5 billion from the previous fiscal year.

**Exhibit 6
Statewide Revenues – All Governmental Funds
2010-11 and 2011-12 Fiscal Years**

Governmental Fund Type	2010-11 Amount	2010-11 Percent of Total	2011-12 Amount	2011-12 Percent of Total	Increase/ (Decrease)	Percent Increase/ (Decrease)
General Fund	\$ 18,477,857,759	69.58%	\$ 17,822,854,462	74.24%	\$ (655,003,297)	-3.54%
Other Funds	8,077,318,944	30.42%	6,182,920,817	25.76%	(1,894,398,127)	-23.45%
Total	\$ 26,555,176,703	100.00%	\$ 24,005,775,279	100.00%	\$ (2,549,401,424)	-9.60%

Exhibit 7 shows total governmental fund type revenues reported by school districts for the 2011-12 and 2010-11 fiscal years by revenue source.

**Exhibit 7
Revenues by Source - All Governmental Funds
2010-11 and 2011-12 Fiscal Years**

Sources	2010-11 Amount	2010-11 Percent of Total	2011-12 Amount	2011-12 Percent of Total	Increase/ (Decrease)	Percent Increase/ (Decrease)
Federal	\$ 4,819,689,609	18.15%	\$ 3,157,525,877	13.15%	\$ (1,662,163,732)	-34.49%
State	9,435,202,650	35.53%	9,079,185,050	37.82%	(356,017,600)	-3.77%
Local	12,300,284,444	46.32%	11,769,064,352	49.03%	(531,220,092)	-4.32%
Total	\$ 26,555,176,703	100.00%	\$ 24,005,775,279	100.00%	\$ (2,549,401,424)	-9.60%

The \$2.5 billion decrease in total revenues for the 2011-12 fiscal year consisted of a net decrease in Federal revenues of \$1.7 billion, a decrease in State revenues of \$356 million, and a decrease in local revenues of \$531 million. Total Federal, State, and local revenues decreased by 34.49, 3.77, and 4.32 percent, respectively. The significant decrease in Federal revenues is due primarily to the termination of certain ARRA and other Federal stimulus funding. The decrease in State revenues consists of a decrease of \$183 million in State FEFP revenues and a decrease of \$173 million in restricted State revenues. The decrease in local revenues is due primarily to a decrease in the local effort required by the State to be levied by school districts, which decreased from \$7.2 billion for the 2010-11 fiscal year to \$6.9 billion for the 2011-12 fiscal year.

Exhibit 8 shows Federal, State, and local sources reported in the general fund (operating fund) of school districts for the 2011-12 and 2010-11 fiscal years.

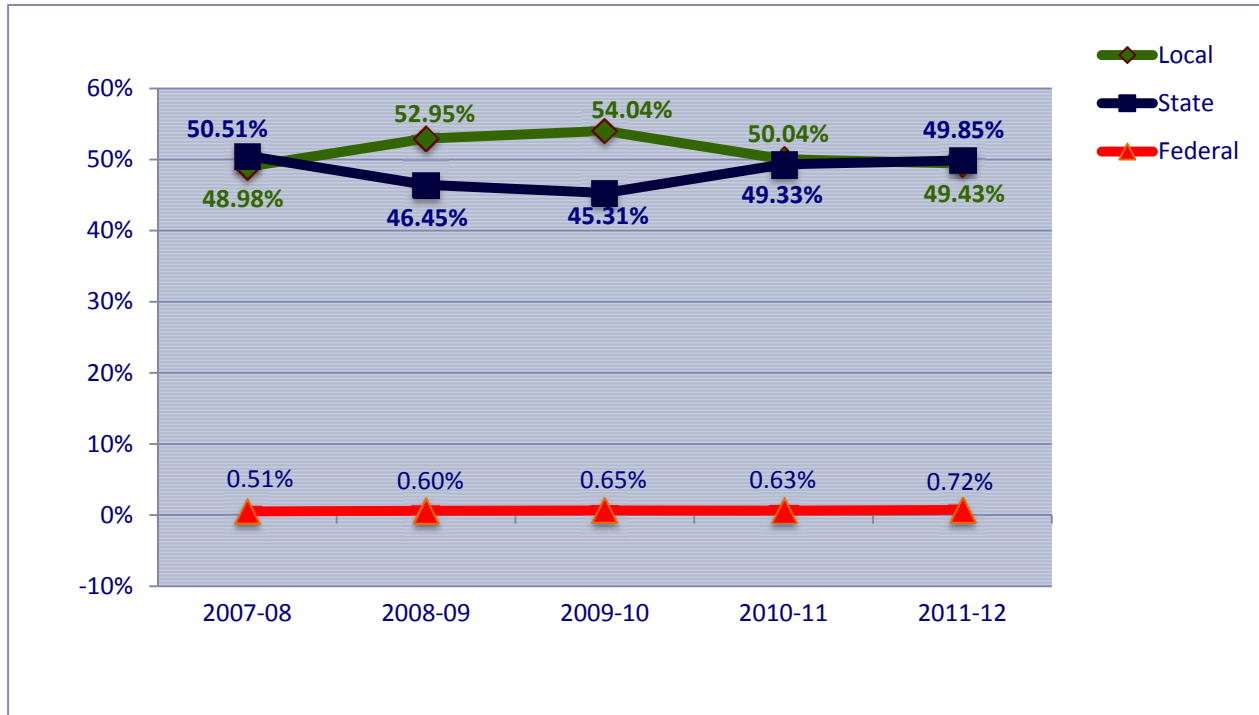
**Exhibit 8
General Fund Revenues by Source
2010-11 and 2011-12 Fiscal Years**

General Fund	2010-11 Amount	2010-11 Percent of Total	2011-12 Amount	2011-12 Percent of Total	Increase/ (Decrease)	Percent Increase/ (Decrease)
Federal	\$ 116,869,376	0.63%	\$ 127,531,840	0.72%	\$ 10,662,464	9.12%
State	9,115,454,054	49.33%	8,886,112,029	49.85%	(229,342,025)	-2.52%
Local	9,245,534,330	50.04%	8,809,210,593	49.43%	(436,323,737)	-4.72%
Total	\$ 18,477,857,760	100.00%	\$ 17,822,854,462	100.00%	\$ (655,003,298)	-3.54%

As shown on Exhibit 8, the State provided 49.85 percent of general fund resources during the 2011-12 fiscal year, while local revenue sources provided 49.43 percent of total general fund resources. As discussed later in this section of the report, Federal funds are restricted and most of those funds are reported in the school districts' special revenue

funds. The percentage of revenues from Federal, State, and local sources in the general fund over the last five fiscal years can be seen on Exhibit 9:

**Exhibit 9
Percentage of General Fund Revenues from Federal, State,
and Local Sources for 2007-08 Through 2011-12 Fiscal Years**



The majority of the State and local resources for school district operations are derived from FEFP, which is designed to provide a base level of educational resources per FTE for all school districts. FEFP moneys are primarily generated by multiplying the number of FTE students in funded educational programs by various weights and cost factors determined by the Legislature to determine base funding from State and local FEFP funds. Each school district receiving State FEFP moneys must levy the required local effort millage in its local property taxes.

State and local FEFP revenue for school district operations totaled \$12.48 billion for the 2011-12 fiscal year, comprised of \$5.54 billion in State revenues and \$6.94 billion in local revenues. In addition to the \$5.54 billion in State revenues for operations as part of the FEFP, the school districts reported \$3.54 billion in restricted State revenues. These restricted State revenues were for Class Size Reduction, Workforce Development, School Recognition, and other specific programs.

In addition to the \$6.94 billion in local revenues for funding operations as part of the FEFP, the school districts reported \$4.8 billion in other local revenues. These local revenues included, but were not limited to, \$1.94 billion from capital outlay millage levies for advertised construction, facility maintenance, and equipment; \$923 million from discretionary local effort millage levies for operations; \$199 million from special voter levies; \$58 million from critical needs operation levies; and \$54 million from debt service millage levies for servicing debt. Additional sources of local revenue included sales taxes, impact fees, charges for services, investment income, and other local sources. Twenty-two school districts reported local sales tax revenue totaling \$445 million for the 2011-12 fiscal year, which is comparable to 22 school districts that reported \$465 million for the previous fiscal year. Twenty-nine school districts

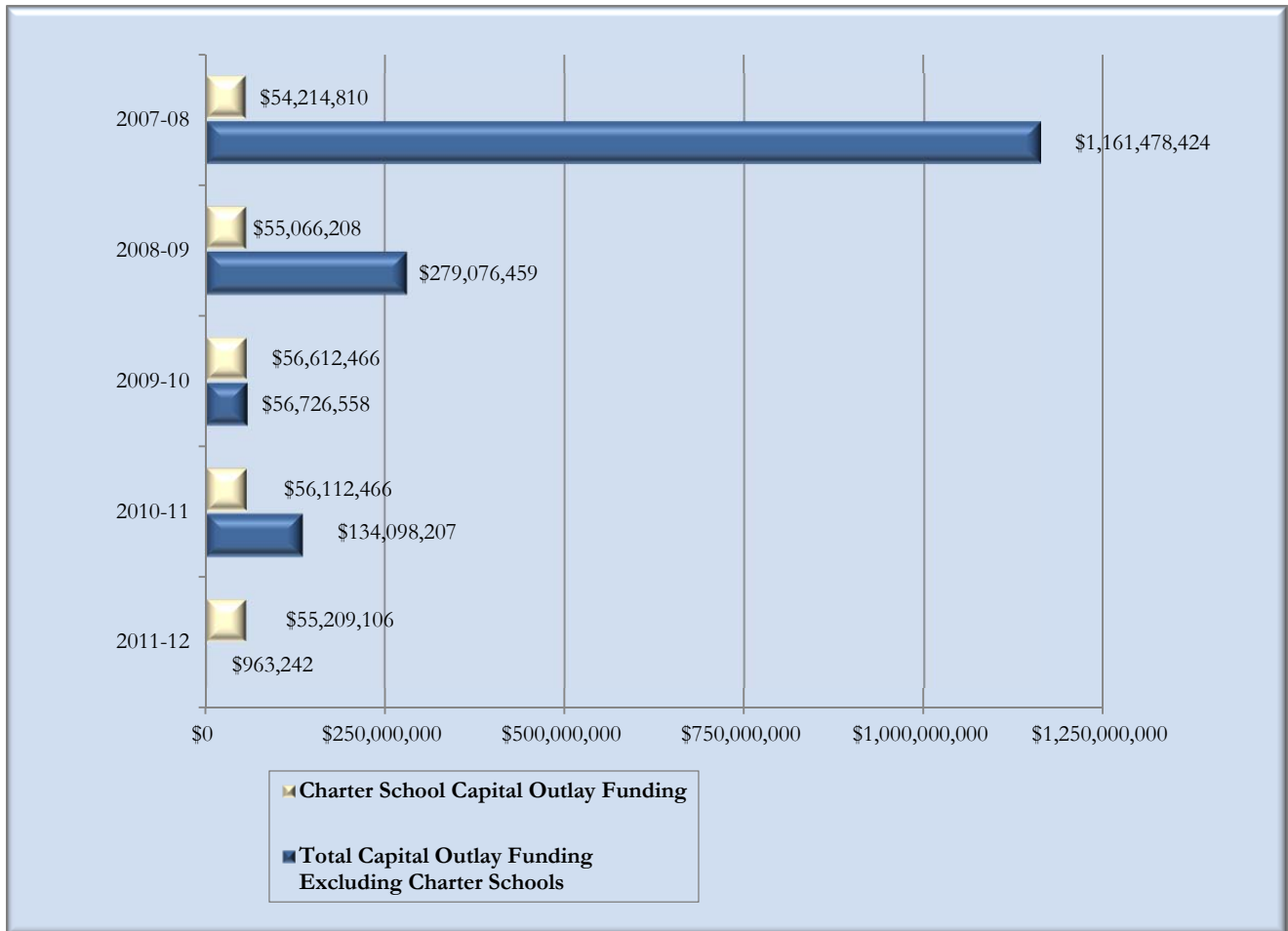
reported impact fee revenue totaling \$102 million for the 2011-12 fiscal year as compared to 36 school districts that reported \$88 million for the previous fiscal year.

Resources of the special revenue funds consist of moneys restricted by Federal and State grantors to be used for specific program purposes, such as Federal Title I and National School Lunch Act revenues. Because these resources are restricted, school districts can use them only for those specific activities that meet the purposes of the granting agency, and such resources are not available for general appropriation for operating activities or for unexpected events or emergencies.

The issuance of long-term debt is a significant source of capital funding for school districts. Proceeds associated with the issuance of debt (net of refundings) in the 2011-12 fiscal year totaled \$40 million as compared to \$633 million in the 2010-11 fiscal year. Within the governmental funds, debt service and capital projects funds are used to account for resources restricted specifically for the payment of debt and for the acquisition of real property and the construction, renovation, remodeling, and maintenance of school district facilities. These resources are generally not available to finance the operating activities of a school district.

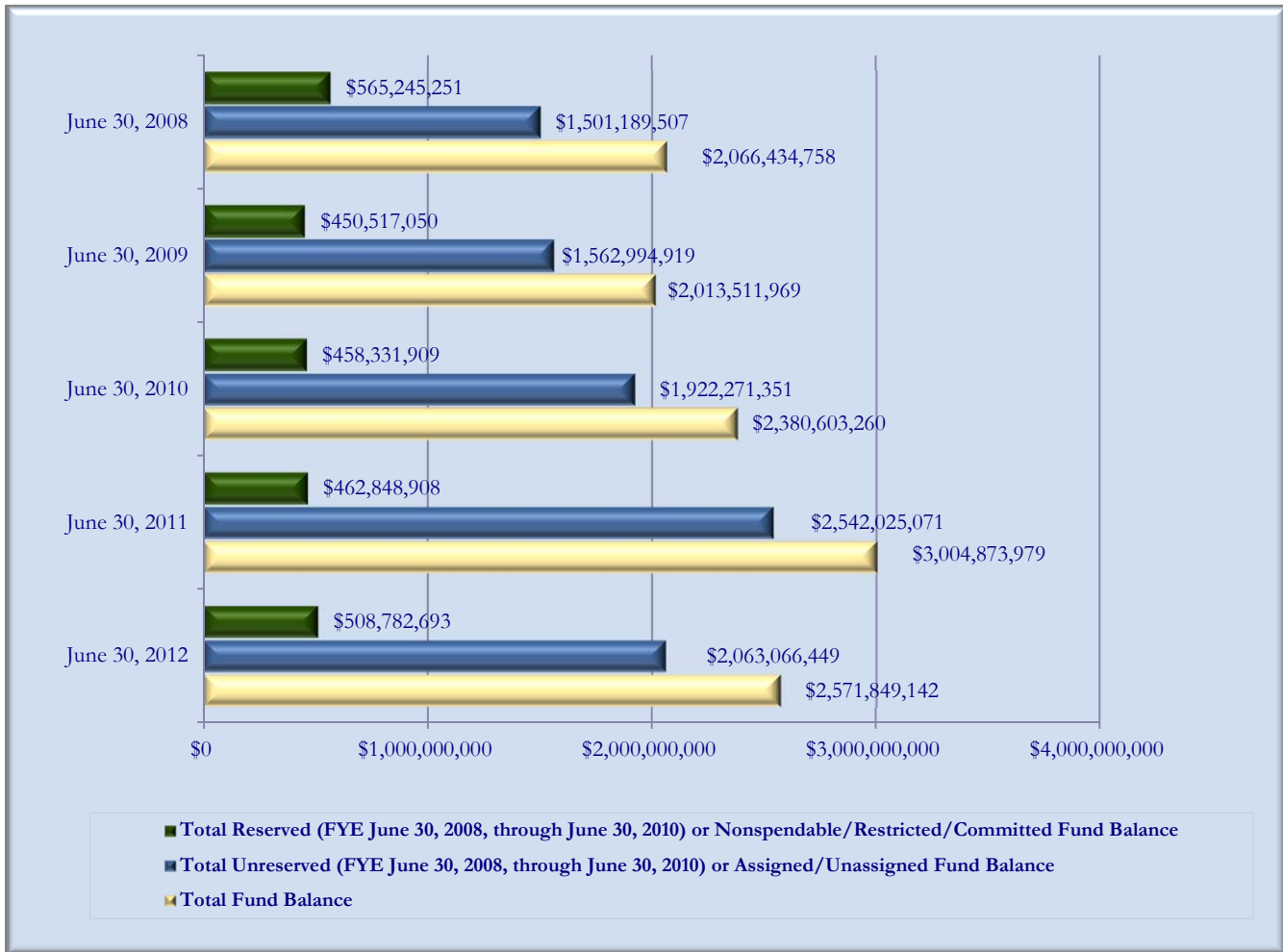
Until recently, certain statutory appropriations, such as Public Education Capital Outlay (PECO) appropriations authorized by Section 1013.65, Florida Statutes, constituted significant funding for school district new construction and facilities maintenance projects. These statutory appropriations included, but were not limited to, PECO, Classrooms First, Classrooms for Kids, and Class Size Reduction, which were predominantly funded using proceeds from the gross receipts tax established by Section 9(a)(2), Article XII and 11(d), Article VII of the State Constitution. As shown on Exhibit 10, these appropriations to school districts, excluding charter schools, have decreased from \$1.2 billion for the 2007-08 fiscal year to \$983 thousand for the 2011-12 fiscal year. During the same time period, capital outlay funding for charter schools has remained relatively constant, increasing slightly from \$54.2 million for the 2007-08 fiscal year to \$55.2 million for the 2011-12 fiscal year.

Exhibit 10
State Capital Outlay Appropriations
for 2007-08 Through 2011-12 Fiscal Years



Fund Balance Trends. As shown below on Exhibit 11, the combined fund balances of the general funds (operating funds) of school districts Statewide increased from \$2.07 billion for the 2007-08 fiscal year to \$2.57 billion for the 2011-12 fiscal year.

**Exhibit 11
Fund Balances of the General Fund³ for the
Fiscal Years Ended June 30, 2008, Through June 30, 2012**



Decreases of 10,000 and 18,600 in student enrollment Statewide were noted for the fiscal years ended June 30, 2008, and June 30, 2009, respectively, and a decline of \$52.9 million in total fund balance was noted for the fiscal year ended June 30, 2009. The percentage of unreserved or assigned/unassigned fund balance to total fund balance ranged from a low of 72.7 percent for the fiscal year ended June 30, 2008, to a high of 84.6 percent for the fiscal year ended June 30, 2011.

Total fund balance decreased by \$433 million from June 30, 2011, to June 30, 2012, primarily from reductions of State and local revenues discussed in the **Funding Trends** section. Additionally, in the 2009-10 and 2010-11 fiscal years, certain instructional costs were shifted to the special revenue funds where these costs were paid from Federal funds

³ For comparison purposes, unassigned/assigned fund balance classification pursuant to GASB Statement No. 54 is similar to unreserved fund balance used in the presentation of the fund balance of the general fund prior to the 2010-11 fiscal year. See Exhibits 12 and 13. Also, for comparison purposes, nonspendable/restricted/committed fund balance classification pursuant to GASB Statement No. 54 is similar to reserved fund balance used in the presentation of the fund balance of the general fund prior to the fiscal year ended June 30, 2011.

such as ARRA, as mentioned in the **Financial Condition Trends** section. However, as discussed in the **American Recovery and Reinvestment Act and Other Federal Funding** section, with the exception of the Race-to-the-Top Incentive and School Improvement grants, most ARRA funding terminated during the 2010-11 fiscal year. An expected increase in the per FTE FEFP allocation for the 2012-13 fiscal year may mitigate further fund balance decreases for the 2012-13 fiscal year.

Financial Condition Background

Financial Condition Measure. There are several measures that may be used to evaluate the financial condition of governments. One widely used financial condition measure that is relevant to school districts compares the level of available equity in the operating fund to overall operating resources for that fund for a fiscal year. This measure shows the net accumulated resources at a point in time that is available for appropriation to meet the costs of unexpected and nonrecurring events. We used this measure in analyzing school district financial condition (see Exhibits 12 and 13).

Exhibit 12
Financial Condition Measure, pre-GASB 54

<u>General Fund Unreserved Fund Balance</u> ⁴	=	Financial Condition Ratio (%)
General Fund Total Revenues		

Exhibit 13
Financial Condition Measure, post-GASB 54

General Fund Total Assigned <u>and Unassigned Fund Balance</u>	=	Financial Condition Ratio (%)
General Fund Total Revenues		

Credit rating agencies generally look more favorably on financial condition ratios of at least 5 percent. Other literature suggests percentages ranging from 5 to 10 percent. However, often the guidance is not clear as to whether the percentage is derived from total fund balance or assigned and unassigned fund balance (previously reported as unreserved fund balance). We also considered revenue stream characteristics and expenditure practices for school districts. In view of the revenue and expenditure considerations of school districts, the established financial management practices followed by school districts, and the oversight by the FDOE, a lower total assigned and unassigned fund balance threshold may be reasonable without unacceptable risks.

AUDIT FINDINGS

Classification of Audit Findings

Auditing standards require that auditors report material weaknesses in internal control and significant control deficiencies that are disclosed during the course of a financial statement audit. A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the financial statements would not be prevented, or detected and corrected on a timely basis. A

⁴ For comparison purposes, unreserved fund balance is similar to unassigned/assigned fund balance classification pursuant to GASB Statement No. 54 in calculating the financial condition ratio prior to the fiscal year ended June 30, 2011.

significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. Auditors must also report material noncompliance or abuse that has a material effect on the audit. The classification of an audit finding is dependent upon its potential impact on the specific school district under audit. Therefore, the classification of an audit finding could vary from school district to school district.

The audit reports for 5 school districts contained no findings, while audit reports for the remaining 62 school districts included a total of 467 findings addressing weaknesses in internal control; instances of noncompliance with applicable laws, rules, or regulations; or additional matters. For purposes of this report, audit findings are generally classified in one of three categories. The first category consists of material weaknesses, as defined above, and instances of material noncompliance. Noncompliance with applicable laws or rules is considered material when it is determined that the noncompliance could have a direct and material effect on the determination of financial statement amounts. The second category consists of significant deficiencies as defined above, instances of noncompliance with applicable laws or rules, or additional matters that should be addressed by management. The third category includes instances of internal control deficiencies related to Federal awards or noncompliance with Federal awards requirements.

In the audit reports issued by our office, all audit findings are included within the body of the audit report. In the audit reports issued by the other independent CPAs, material weaknesses and significant deficiencies are identified within the body of the report, and additional matters are generally included in a separate management letter within the audit report.

Financial Statement Material Weakness and Material Noncompliance Findings

The audit reports for eight school districts (Bay, DeSoto, Franklin, Glades, Jackson, Manatee, Okeechobee, Washington) included findings that were considered to be material weaknesses, and the report for one of the school districts (Manatee) also cited instances of material noncompliance. This represents an increase compared to the five audit reports that included material weaknesses for the previous fiscal year, none of which had instances of material noncompliance. Pursuant to Section 1003.621(1)(a)3., Florida Statutes, a school district cited with a material weakness or instance of material noncompliance in a financial audit is ineligible for recognition as an academically high-performing school district. Academically high-performing school districts are granted more flexibility than other school districts in meeting the specific requirements of Florida statutes and State Board of Education rules.

The material weakness and material noncompliance findings contained in the eight school district audit reports are described below.

- For six school districts (Bay, DeSoto, Franklin, Glades, Jackson, Washington), material weaknesses addressed procedural enhancements needed to ensure the accuracy and completeness of the financial statements.
- For two school districts (Glades, Manatee), material weaknesses addressed the use of capital outlay tax levies for purposes not authorized by law, resulting in questioned costs of \$314,353 for one school district (Glades) and \$919,000 for the other school district (Manatee). For one school district (Manatee), the tax levy use was reported as material noncompliance with Florida law.
- For one school district (Manatee), a material weakness addressed procedures that caused a continual decline in financial condition. The school district's general fund total assigned and unassigned fund balance decreased by \$8.7 million from a \$3.7 million surplus at June 30, 2011, to a \$5 million deficit at June 30, 2012. Pursuant to Section 1011.51, Florida Statutes, the school district's superintendent notified the school board and the FDOE that the financial condition ratio was projected to fall below 3 percent, and the school district's fiscal recovery plan was submitted to the FDOE. Deficits were also reported in the school district's two self-insurance internal service funds.

This school district (Manatee) also had a budgetary control deficiency that was reported as material noncompliance with Florida law. Contrary to law, the school district did not plan expenditures for various programs and certain employee compensation and did not appropriately monitor the budget to actual expenditures throughout the fiscal year to assist in identifying budget deficits. These deficiencies were not conducive to effective management control over the school district's resources and may have contributed to weaknesses in the school district's financial condition.

- For one school district (Okeechobee), a material weakness addressed collection procedures for school internal funds.

Financial Statement Significant Deficiency and Additional Matter Findings

The audit reports for five school districts contained no audit findings, and reports for the remaining 62 school districts included findings that addressed control deficiencies; instances of noncompliance with applicable laws, rules, and regulations; or additional matters. The following is a summary of those findings.

Financial Condition. In addition to the material weakness discussed previously for Manatee County School District, audit reports for four school districts included findings addressing the school districts' financial condition, as follows:

- Two school districts reported declines of \$2.6 million and \$394,673, respectively, in the districts' ending general fund total assigned and unassigned fund balances for the fiscal year, and the ending general fund total assigned and unassigned fund balances represented 1.62 and 2.13 percent of general fund total revenues, respectively. One of the two school districts subsequently projected that the school district's financial condition ratio would also fall below 2 percent due to declining enrollment and related loss of revenues. Pursuant to Section 1011.51, Florida Statutes, superintendents of these school districts notified the school boards and the FDOE, and also prepared budget action plans, which the FDOE indicated may reasonably help the school districts avoid financial emergency in the 2012-13 fiscal year.
- For one school district, the ending general fund total assigned and unassigned fund balance at June 30, 2012, was 3.4 percent of general fund total revenues. However, as of December 31, 2012, the school district projected that the June 30, 2013 fiscal year end general fund total assigned and unassigned fund balance would decline to 2.85 percent of the general fund total budgeted revenues. Consequently, the school district notified the school board and the FDOE of the financial condition and the school district's fiscal recovery plan.
- For one school district, the ending general fund total assigned and unassigned fund balance was 5.5 percent of general fund total revenues at June 30, 2012; however, the ending general fund total assigned and unassigned fund balance could be further reduced below 3 percent if the school district is required to repay questioned costs and additional board premium contributions are required for the school district's health and workers' compensation self-insurance program.

Under these circumstances, these school districts have less resources available for emergencies and unforeseen situations than other school districts and were at a higher risk of experiencing financial difficulty.

Information Technology. For 43 school districts, various control deficiencies in information technology (IT) were noted, as discussed below:

- **Data Loss Prevention.** Twenty-eight school districts needed improvements in security controls over data loss prevention. Effective data loss prevention helps ensure protection from unauthorized disclosure through the establishment of procedures to identify and classify confidential or sensitive data, locate the storage and pathways of confidential or sensitive data, and monitor the use and transmission of confidential or sensitive data.

- **Access Controls.** Twenty-four school districts had various deficiencies in IT access controls. For example, at certain school districts, inappropriate or unnecessary access privileges existed, data was not classified according to sensitivity or level of significance, or documentation of user access authorization was not maintained. School district management was notified of the specific details of the access control deficiencies, although the details were not always included in the audit reports to avoid the possibility of compromising school district data and IT resources.
- **Security Incident Response Plans.** Twenty-one school districts lacked or needed enhancements in written security incident response plans. Computer security incident response plans are established by management to ensure an appropriate, effective, and timely response to computer security incidents. These written plans typically detail responsibilities and procedures for identifying, logging, and analyzing security violations and include a centralized reporting structure, provision for designated staff to be trained in incident response, and notification of the affected parties.
- **Logging/Monitoring.** Thirteen school districts had inadequate logging or monitoring of data and IT resources.
- **Lack of Timely Termination of Access.** Twelve school districts lacked timely termination of former employee IT access privileges.
- **Written Policies.** Twelve school districts lacked written IT policies and procedures for certain important IT control functions.
- **Disaster Plans.** Nine school districts needed improvements in disaster preparedness and recovery plans or the plans needed to be tested.
- **Security Awareness.** Eight school districts needed security awareness training programs or improvements in already existing security awareness training programs.
- **Risk Assessment.** Seven school districts had not developed written, comprehensive IT risk assessments. IT risk assessments, including the identification of risks and the evaluation of the likelihood of threats and the severity of threat impact, help support management's decisions in establishing cost-effective measures to mitigate risk and, where appropriate, formally accept residual risk.

Record Keeping/Records Management. In addition to the material weaknesses in financial reporting procedures discussed previously for Bay, DeSoto, Franklin, Glades, Jackson, and Washington County School Districts, the audit reports for 30 school districts included findings addressing the need for improvements in certain record keeping and financial records management procedures. At 21 school districts, procedures needed improvement to ensure the accuracy and completeness of the financial statements. While many of these findings related to required audit adjustments for the accuracy of the financial statements, other instances included needed improvements in the preparation and accuracy of the Schedule of Expenditures of Federal Awards; inadequate disclosure in the notes to financial statements; lack of reconciliations between detailed supporting documentation and general ledger accounts; lack of formal procedures for the year-end financial statement close-out process; and needed improvements in procedures for identifying major governmental funds in the financial statements.

For three school districts, deficiencies were noted in accountability over fuel and food service inventories. Also, audit reports of three other school districts included the need for enhancements in controls over journal entries. Three school districts reported unrestricted capital outlay resources ranging from \$1.6 million to \$5 million in capital projects funds, without officially designating the employee that had the authority to express the intended use of the funds, and school district records did not evidence the specific intended use of these funds. Other findings and recommendations addressed the lack of an actuarial valuation to support a reported liability, enhancements needed in budget process monitoring, needed improvements in timely and prominently posting required budget information on school districts' web sites, and school board minute procedures.

Cash and Investment Controls. For 29 school districts, findings and recommendations addressed control deficiencies over cash or investments and, for 19 school districts, improvements were needed in controls over electronic funds transfers (EFTs). Deficiencies noted included the lack of school board-approved policies and procedures prescribing EFT accounting and controls, contrary to State Board of Education Rule 6A-1.0012, Florida Administrative Code (FAC); EFT agreements with banks that omitted critical information, such as the names and signatures of employees authorized to initiate EFTs; EFT agreements that authorized former employees to make EFTs; and EFT agreements or school district procedures that did not provide for appropriate separation of duties.

Audit reports also noted that improvements in controls were needed over central cashier and decentralized collections, such as food service collections and school child care program fees collections, at seven school districts. Improvements in bank reconciliation procedures for six school districts were needed, and three school districts needed to improve controls over investments.

Capital Assets Management. For four school districts, findings and recommendations addressed deficiencies in the accountability for long-lived assets, including land, improvement other than buildings, buildings and fixed equipment, and tangible personal property. For three school districts, deficiencies were noted in tangible personal property accountability procedures, such as untimely tagging property to indicate school district ownership, inadequately documenting or updating property records for acquisitions or dispositions, and the lack of adequate physical inventory procedures. In addition, the audit report for one school district addressed the lack of adequate detailed subsidiary records for capital assets.

Expenditures/Purchasing. For 20 school districts, findings addressed the need to improve controls over purchasing practices and operating expenditures. For ten school districts, improvements were needed in controls over purchasing cards, such as monitoring of purchasing card credit limits, reviews and approvals of purchasing card charges prior to payments, and procedures for cancelling terminated employees' card accounts. For ten school districts, controls needed to be enhanced over contract monitoring procedures to ensure that payments are consistent with contract terms and conditions. Four school districts did not comply with competitive selection requirements of State Board Education Rule 6A-1.012, FAC, for various contractual service contracts. In addition, auditors of two school districts noted that controls over issuing and approving purchase orders needed enhancement.

Payroll and Personnel. For 45 school districts, findings addressed the need to improve controls over payroll and personnel, as summarized below:

- **Compensation.** For 34 school districts, school boards had not adopted formal policies and procedures to ensure that the differentiated pay process of certain school district employees had been properly documented using the factors prescribed in Section 1012.22(1)(c)4., Florida Statutes.
- **Personnel Administration.** For seven school districts, improvements were needed in controls over various areas of personnel administration. For example, for four school districts, procedures for performing background screenings or rescreening for employees and contracted vendors with direct student contact were not adequate. Other control deficiencies noted included the inadequate documentation for new hires, procedures needed for properly classifying an employee as an independent contractor, and the need for improved controls over employee performance assessment.
- **Payroll Processing.** For seven school districts, controls over payroll processing could be enhanced. At six of these school districts, auditors noted that procedural enhancements could be made to sufficiently and appropriately evidence employee work time supporting salary and benefits costs. For two school districts, procedural enhancements were needed to ensure that employee overtime is properly approved, documented, and accurately recorded.

- **Other.** For four school districts, improvements were needed in school district policies and procedures related to accrued leave time and calculations of terminal leave payments to ensure consistency with Florida law. For one of the school districts, auditors noted approximately \$34,000 in vacation terminal leave payments that were in excess of the 60-day statutory limit for the 2011-12 fiscal year, and \$30,000 for the 2012-13 fiscal year. At two school districts, employment agreements for superintendents included severance pay provisions that allowed for severance pay that exceeded 20 weeks of salary, contrary to Section 215.425(4)(a), Florida Statutes.

Insurance. In addition to the material weakness previously discussed for self-insurance fund deficits at Manatee County School District, audit reports for nine school districts included findings addressing the need to improve controls over the administration of self-insurance plans. For five school districts, auditors noted that controls needed improvements over monitoring third party administrators of the self-insurance plans. For example, control deficiencies included no review of service organization reports to ensure that the third party administrators had appropriate internal controls in place; no review and related determination of the reasonableness of assumptions used by the third party specialists; and the need for periodic reviews by the school districts of insurance claims paid by the third party administrators. Also, two other school districts needed to establish formal policies and procedures to monitor the financial condition of the self-insurance plans and ensure that favorable net asset balances were maintained.

Capital Construction and Related Expenditures. Findings addressed the need to improve controls over construction and capital outlay expenditures for 24 school districts, as summarized below:

- **Construction Planning.** For 14 school districts, procedural enhancements were needed related to construction planning, alternative construction methods and maintenance techniques, and accountability for facilities and maintenance departments' accountability. These school districts needed to establish long-range facilities planning committees comprised of various stakeholders to periodically meet and assist school district facilities personnel in identifying long-range construction needs; develop written policies and procedures requiring periodic evaluations of alternative facilities construction methods and techniques for performing significant maintenance-related jobs; or develop additional goals and objectives for the facilities planning and maintenance departments to identify efficiency or cost effectiveness outcomes for department personnel.
- **Construction Monitoring.** For eight school districts, improvements were needed in controls over construction management, guaranteed maximum price, and subcontractor contracts.
- **Acquiring Professional Services.** Two school districts did not comply with Section 287.055, Florida Statutes, when procuring construction management services.
- **Restricted Capital Outlay Resources.** In addition to the material weakness previously discussed for Glades County School District and the material weakness and material noncompliance previously discussed for Manatee County School District, findings addressed control deficiencies over restricted capital outlay resources as summarized below:
 - For 15 school districts, contrary to law, restricted capital outlay moneys in amounts ranging from \$9,321 to \$3.3 million were used for unallowable purposes, such as premiums for certain types of insurance not directly related to educational or ancillary plants, instructional software purchases or software maintenance fees, debt payments, landscaping, custodial costs, gasoline, and copier supplies.
 - Three school districts did not adequately advertise the intended uses of ad valorem tax levy proceeds, resulting in questioned costs ranging from \$12,179 to \$299,300.
 - Three school districts needed to resolve the previous fiscal year appropriated Public Education Capital Outlay or Classroom First Funds questioned costs, ranging from \$164,294 to \$341,000, which were subject to reversion to the State pursuant to Section 216.301(2), Florida Statutes.

Adult General Education Classes. Chapter 2011-69, Laws of Florida, Specific Appropriation 96, provides that each school district shall report enrollment for adult general education programs identified in Section 1004.02, Florida Statutes, in accordance with the FDOE instructional hours reporting procedures. The audit reports for 25 school districts included findings that the school districts could enhance controls over enrollment reporting. Since future funding may be based, in part, on enrollment data reported to the FDOE, it is important that such data be reported correctly to the FDOE.

Charter School Monitoring. For three school districts, findings and recommendations addressed the need to enhance monitoring of charter schools, including review and approval of charter school applications; the lack of contract provisions related to charter schools timely providing financial statements and annual audit reports to their sponsoring school districts; and the need to enhance procedures related to terminated charter schools, including reconciling property to related records and timely reversion of unencumbered funds.

Miscellaneous Findings. In addition to those findings described above, audit findings addressing various other matters, although not predominant, were included in the individual school district audit reports. These matters included, for example, the insufficiency or lack of formal fraud policies; the need for improved controls over social security numbers to ensure compliance with Section 119.071(5)(a), Florida Statutes; noncompliance with educational facility safety standards; the use of workforce development funds for purposes contrary to Chapter 2011-69, Laws of Florida or the need for a spending plan for the use of unspent funds; the lack of controls over wireless devices; the need for enhancement over food vending machine sales; deficiencies in procedures for assessing student fees; deficiencies in internal controls over high school student diplomas; the lack of timely debt payments; and direct-support organization audits not conducted in accordance with *Government Auditing Standards*, contrary to Rules of the Auditor General.

Federal Awards Findings

For 34 school districts, findings addressed control deficiencies over Federal awards and Federal noncompliance. Material noncompliance and material internal control weaknesses related to Federal programs were noted at six school districts (Gadsden, Lafayette, Manatee, Pinellas, Putnam, Sarasota). These material Federal findings addressed noncompliance with the Federal compliance requirements of Allowable Costs/Cost Principles; Matching, Level of Effort, and Earmarking; and Special Tests and Provisions; and related to major programs including the National School Lunch and Breakfast; Even Start; Exceptional Student Education; Federal Pell Grant; Education Technology; and Improving Teacher Quality programs. Other Federal findings that were not considered material noncompliance addressed various Federal compliance requirements for the National School Lunch and Breakfast; Exceptional Student Education; Race-To-The-Top; Title I; Federal Pell Grant; School Improvement Grants, and other programs. As previously discussed in the **American Recovery and Reimbursement Act and Other Federal Funding** section of this report, ARRA mandates special accountability and transparency requirements regarding Federal economic stimulus funds, which requires additional record keeping for school districts and expanded audit procedures for auditors.

Repeated Findings From Prior Fiscal Years

A significant number of findings included in audit reports for the 2011-12 fiscal year were also included in previous audit reports. Of the 467 findings included in the 2011-12 fiscal year audit reports reviewed, 107 (23 percent) were repeated from previous audit reports for at least two consecutive fiscal years. The percentage of repeated findings indicates that some school districts did not take action to timely correct prior year deficiencies or noncompliance.

Pursuant to Section 218.39, Florida Statutes, on September 13, 2013, we notified the Legislative Auditing Committee of 50 district school boards that failed to take full corrective action in response to one or more recommendations included in the two preceding audit reports.

OTHER MATTERS OF INTEREST

School District Budget Transparency

Section 1011.035, Florida Statutes, requires each district school board to post on its Web site a plain language version of each proposed, tentative, and official budget describing each budget item in easily understandable terms. The statute includes a list of items recommended for inclusion on the Web sites, such as budget hearing information, contracts with teachers' unions and noninstructional staff, and contracts with vendors exceeding \$35,000. This statutory requirement will enable taxpayers, parents, and education advocates to obtain school district budget and related information in a manner simply explained and easily understandable. Budgetary transparency leads to more responsible spending, more citizen involvement, and improved accountability.

Pursuant to Section 11.45(7)(i), Florida Statutes, on July 9, 2013, we notified the President of the Senate, the Speaker of the House of Representatives, and the Chief Financial Officer of the Florida Department of Financial Services that two school districts (Clay, Lafayette) were reported for noncompliance with Section 1011.035(2), Florida Statutes.

OBJECTIVES, SCOPE, AND METHODOLOGY

The objective of this project was to identify significant financial trends and findings based on our review of school district audit reports.

The scope of this project included a review of the audit reports for the 47 school districts audited by our office and the 20 school districts audited by other independent CPAs for the fiscal year ended June 30, 2012.

Our audit methodology included a review of applicable audit reports and a compilation of significant financial trends and findings. We conducted this review in accordance with applicable generally accepted government auditing standards. We believe that the procedures performed provide a reasonable basis for the summaries of significant financial trends and findings included in this report.

AUTHORITY

Pursuant to the provisions of Section 11.45(7)(f), Florida Statutes, I have directed that this report be prepared to present the summary of financial trends and significant findings identified in district school board audit reports for the fiscal year ended June 30, 2012.



David W. Martin, CPA
Auditor General

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